INDEX.

Subject Index.

	Page
Statement of facts	2
The issue involved	2
Statutes involved and brought in question	2
Synopsis of argument	4
Argument	4

Table of Cases Cited.

Bankers Trust Company v. Bowers, 23 Fed. Rep. (2d) 941	5, 12
Bingham et al. v. Long, 249 Mass. 79, 144 N. E. 77	12
Brewster v. Gage, 280 U. S. 327	5
Eisner v. Macomber, 252 U. S. 189, 64 L. Ed. 521	9
Elmhirst v. United States, 38 Fed. Rep. (2d) 915, cert. denied 282 U. S. 851	5, 11, 17
Goodrich v. Edwards, 255 U. S. 527	8
McCann v. United States, 48 Fed. Rep. (2d) 446	21
McKinney v. United States, 62 Court of Claims 180, cert. denied 273 U. S. 716	5, 15
Myers v. United States, 51 Fed. Rep. (2d) 145	5, 21
Nichols v. United States, 64 Court of Claims 241	5
United States v. Flannery, 268 U. S. 98	8
Walsh v. Brewster, 255 U. S. 536, 41 S. Ct. 392, 65 L. Ed. 762	8

Statutes Cited.

40 Stat. 1065, Section 202 (a), Revenue Act of 1918	2, 6
42 Statutes at Large 227, Section 202, Revenue Act of 1921	3
42 Statutes 237, Section 213	4
43 Statutes at Large 258, Section 204 (a), (b), Revenue Act of 1924	3
43 Statutes at Large 258, Section 204 (c), Revenue Act of 1924	4
42 Statutes 246, Section 219	4
43 Statutes 275, Section 219	4
43 Statutes 256, Section 203	4

Miscellaneous.

Article 343, Regulations 65 and 69	6
Article 343, Regulations 45 and 62	7
Treasury Department 4011, 4012 and 4010, XI-1 Cumulative Bulletin 77, 248 and 249	7
Treasury Department 4177, VII-2 Cumulative Bulletin 134	7

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. 602

CAVOUR HARTLEY, EXECUTOR OF THE ESTATE OF G. G. HARTLEY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE.

BRIEF ON BEHALF OF PETITIONER.

This case comes before the Court on a writ of certiorari issued to the United States Circuit Court of Appeals for the Eighth Circuit, in accordance with the order entered February 4, 1935 (R. 129), granting the petition that had been filed on December 27, 1934.

The case involves the basis for determining gains or losses from sales of property made by the executor of an estate and depletion or depreciation of such properties. The facts were stipulated before the Board of Tax Appeals and the question was presented to the Board as a question of law whether the true basis of figuring such gains and losses was the "acquisition value to the testa-

tor" as claimed by the executor or the "value at the death of the testator" as claimed by the Commissioner. The Board of Tax Appeals held in favor of the rule of value at the death of the testator and the United States Circuit Court of Appeals for the Eighth Circuit sustained the Board of Tax Appeals. As established by the decisions of the courts, this rule is known as the "old basis", while the rule of "acquisition value" is known as the "new basis".

Statement of Facts.

The testator died January 11, 1922. The petitioner taxpayer is the executor of his estate. The deductions involved were for the year 1923 brought forward to 1924 and for the year 1925 and the returns were therefore made under and the taxes governed by the Revenue Acts of 1921 and 1924. The stipulation of facts and the submission of the question as one of law makes further statement of the facts unnecessary here.

The Issue Involved.

The sole issue presented is whether in estimating gains and losses on sales by an executor or in figuring depletion and depreciation is the true basis, the acquisition value to the testator, or the value at the death of the testator within the meaning of the Revenue Acts of 1921 and 1924.

Statutes Involved and Brought in Question.

Revenue Act of 1918, Section 202 (a) (40 Stat. 1065):

> "That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—

(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and

(2) In the case of property acquired on or after that date (a) the cost thereof; or (b) the inventory value if the inventory is made in accordance with section 203."

Revenue Act of 1921, Section 202 (42 Statutes at Large 227):

"Sec. 202. ~~(a)~~ That the basis for ascertaining the gain derived or loss sustained from a sale or other disposition of property, real, personal, or mixed, acquired after February 28, 1913, shall be the cost of such property; * * *

"(b) The basis for ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March 1, 1913, shall be the same as that provided by subdivision (a);

(1) If its fair market price or value as of March 1, 1913, is in excess of such basis, the gain to be included in the gross income shall be the excess of the amount realized therefor over such fair market price or value;

(2) If its fair market price or value as of March 1, 1913, is lower than such basis, the deductible loss is the excess of the fair market price or value as of March 1, 1913, over the amount realized therefor; and

(3) If the amount realized therefor is more than such basis but not more than its fair market price or value as of March 1, 1913, or less than such basis but not less than such fair market price or value, no gain shall be included in and no loss deducted from the gross income."

Revenue Act of 1924, Section 204 (a) (b) (43 Statutes at Large 258). This 1924 Act does not differ materially from that of 1921 upon this proposition.

The Act of 1924, Section 204, sub-division (c), also fixed the basis for depletion and depreciation the same as provided in (a) or (b) for gain or loss from sales.

The Acts of 1921 and 1924 both specifically provide for taxation of the income of an estate during administration (42 Stat. 246, Sec. 219; 43 Stat. 275, Sec. 219); both include profits from sale of property by the taxpayer in taxable income (42 Stat. 237, Sec. 213; 43 Stat. 256, Sec. 203).

Synopsis of Argument.

I.

The correct basis in determining gains and profits is acquisition cost to the testator.

II.

The judicial history supports this construction.

III.

The departmental construction has followed the judicial decisions and is not entitled to weight.

IV.

The decision below is not sound or in accordance with the weight of authority and is based on fabricated, as distinguished from actual, gains and losses.

ARGUMENT.

The true basis of estimating gains and losses from sales of property by the executor or depletion and depreciation is the acquisition value to the testator and not the value at the death of the deceased.

The courts passing upon this question have differed as to the proper basis for estimating these gains and losses. The

Court of Claims in three decisions has held directly in favor of the rule of acquisition value to the testator.

McKinney v. *United States*, 62 Court of Claims 180 (Certiorari denied, 273 U. S. 716).

Elmhirst v. *United States*, 38 F. (2d) 915 (Certiorari denied 282 U. S. 851).

Myers v. *United States*, 51 F. (2d) 145.

The doctrine was again reaffirmed by the same court in *McCann* v. *United States*, 48 F. (2d) 446.

The Court of Claims in the *Elmhirst* case cited above attached importance to the denial by this Court of the writ of certiorari in the *McKinney* case, as well as in the dissimilar *Nichols* case (*Nichols* v. *United States*, 64 Court of Claims 241. Certiorari denied 277 U. S. 584), as indicating that this Court found no question worthy of review.

Opposed to this line of cases was the decision of a District Court in the Southern District of New York, in the case of *Bankers Trust Company* v. *Bowers*, 23 F. (2d) 941; the decisions, usually with the minority dissenting—as here—of the Board of Tax Appeals and the decision here sought to be reviewed of the Circuit Court of Appeals of the Eighth Circuit. The Circuit Court of Appeals, Eighth Circuit, in the decision involved herein, after discussing the varying decisions, frankly states that "The matter is far from being free from doubt. It seems to us, however, that the predominance is in favor of construing the intent of Congress to be that the basis should be value at death of the decedent." (R. 116-117.)

The Honorable Circuit Court of Appeals in its decision attaches great importance to the expression of this Court in *Brewster* v. *Gage*, 280 U. S. 327, to the effect that in figuring profits upon estates "such gains are calculated in value at date of decedent's death" and rejected petitioner's contention that this statement was *obiter* and merely by way of

argument and while that court recognized that the question involved in the *Brewster* case was different from that here, Mr. Justice Stone declares: "This language was not lightly used and it may not be lightly put aside. Though not spoken as to the matter now before us, we would hesitate to regard it other than as on the very edge of controlling authority." (R. 116). The Board of Tax Appeals in its decision treats the *Brewster* case as decisive (R. 24).

We have then the Honorable Court of Claims profoundly impressed in its later—though not its first—decision in favor of the "new basis" rule, by the denial of writ of certiorari by this Court. While over against this we have the Honorable Circuit Court of Appeals of the Eighth Circuit likewise profoundly impressed by the language used by way of argument by this Court in the *Brewster* v. *Gage*, case.

We have in the repeated decisions of the Court of Claims a strong assertion of that court's certainty as to the correctness of the conclusion arrived at by the court, while we have in the Circuit Court of Appeals the expression of uncertainty but its conclusion that the *predominance* is in favor of the rule of the "old basis" of—value at the death of the testator.

The history of the statute and the interpretation thereof by the courts have been marked by uncertainty and differences. These questions mostly arose in connection with the Revenue Act of 1918, Section 202 (a), 40 Statutes at Large 1065, but the subsequent Revenue Acts of 1921 and 1924 did not materially change the statute in its application to the issue here involved.

This difference and uncertainty is evidenced by the regulations of the Department itself. In the earlier regulations the Department adopted the basis of "value at the date of death of the testator." Article 343, Regulations 65 and 69,

Article 343, Regulations 45 and 62. After the decision of the Court of Claims in the *McKinney* case, *supra*, the Department changed its regulations, making the basis the acquisition value to decedent (or March 1, 1913, value), Treasury Department 4011, 4012 and 4010, XI-1 Cumulative Bulletin 77, 248 and 249. Again upon the coming down of the decision of the Court of Claims in the *Nichols* case, *supra*, the Department, construing the *Nichols* case as overruling the *McKinney* case, changed back to its former basis of value at the death of the testator. Treasury Department 4177, VII-2 Cumulative Bulletin 134. Later the Court of Claims in the *Elmhirst* case emphatically pointed out that it had not overruled the *McKinney* case in the *Nichols* case and with equal emphasis pointed out the vital differences between the two cases. Had the Commissioner not misinterpreted the decision of the Court of Claims in the *Nichols* case and erroneously held that it overruled the *McKinney* case, this case and much of the subsequent litigation would never have been heard of, for the rule had supposedly been settled by the decision of the Court of Claims in the *McKinney* case and by the denial of the writ of certiorari by this Court. The majority (five to four) of the Board of Tax Appeals likewise declined to be bound by the doctrine of the *McKinney* case as laid down by the Court of Claims and adhered to the rule of the value at the death of the testator. The Honorable Federal District Judge in the *Bowers* case, *supra*, likewise was persuaded to refuse to follow the decision of the Court of Claims in the *McKinney* case because he was unable to reconcile the *Nichols* case with that case and believed that the effect of the later case was to overrule the earlier one. This decision of the Honorable District Judge was a year and a half before the Court of Claims had emphatically reasserted the doctrine of the *McKinney* case in the late *Elmhirst* case and differentiated

very fully between the facts, the statute, and the question involved, in the *Nichols* and *McKinney* cases.

The underlying bases for the decisions of the Court of Claims are (a) the idea of "real" "actual" profits as distinguished from "fabricated" or "invented" profits (these very apposite words are the court's, not ours), (b) the identity of the executor with the testator based on the fundamental concept of the common law that the executor is the representative of the deceased—to close the estate, pay the debts, sell the property, if necessary, to pay the debts and to turn over the residue to the heirs.

This theory of "actual profits" as distinguished from technical or invented profits had its genesis in the reasoning of this Court in the *Goodrich, Walsh* and *Flannery* cases, more particularly the *Goodrich* case. See *Goodrich* v. *Edwards,* 255 U. S. 527, 41 S. Ct. 390, 391, 65 L. Ed. 758, and *Walsh* v. *Brewster,* 255 U. S. 536, 41 S. Ct. 392, 65 L. Ed. 762, and *United States* v. *Flannery,* 268 U. S. 98, 101, 45 S. Ct. 420, 69 L. Ed. 865.

These cases emphasise the proposition that in spite of the literal wording of the Revenue Statute fixing the March 1, 1913, value as the basis for figuring gains and losses where the purchase was prior to that date—and the actual cost if purchased after that date—that there must in reality be an *actual* gain, an increase of the selling price, not merely over the March 1, 1913, value but over the prior actual cost; that therefore the statute was not to be read literally and so impose a tax where no actual gain existed even though the selling price be greater than the March 1, 1913, value.

The Honorable Commissioner of Internal Revenue in this *Goodrich* case had ruled that the Act of Congress fixing the March 1, 1913, value as the basis, where property was purchased prior to that date, had capitalized the assets of the taxpayer at their value as it existed on that date and

that the value as of that date must control and that the difference between that value and the higher selling value was income when the sale was made.

The Honorable Solicitor General of the United States, looking deeper into the question, saw that this construction violated the very underlying theory of an income tax as authorized by the 16th Amendment and as defined by this Court in the *Eisner* case (*Eisner* v. *Macomber*, 252 U. S. 189, 64 L. Ed. 521). There Mr. Justice Pitney, in defining income, pointed out that the 16th Amendment must be construed in connection with the tax clauses of the original Constitution and that a proper regard for its genesis, as well as its very clear language, requires that this amendment shall not be extended by loose construction. That the constitutional limitations still have an appropriate and important function and are not to be overridden by Congress or disregarded by the courts. The Honorable Associate Justice adopted the definition of income as already laid down by the court with an additional elucidation of his own, making the definition read as follows:

> "Income may be defined as the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital assets, to which it was applied in the Doyle case (pp. 183, 185)."

Again he continues:

> "Here we have the essential matter: not a gain accruing to capital, not a growth or increment of value in the investment; but a gain, a profit, something of exchangeable value proceeding from the property, severed from the capital, however invested or employed, and coming in, being 'derived,' that is, received or drawn by the recipient (the taxpayer) for his separate use, benefit, and disposal; that is income derived from property. Nothing else answers the description."

With this careful surveying out of the field of income by this Court before him, the Honorable Solicitor General quickly discerned that the rule of the Honorable Commissioner or even the Act of Congress itself, if given the Commissioner's interpretation, would operate to levy a tax upon income that had no substance, no reality, no actuality to it, and he frankly admitted in his brief to this Court that if such construction were adopted "a serious constitutional question arises". "Whatever gains are made by selling property resulted from three acts—acquisition, holding, and selling. These three acts together resulted in a gain or a loss, according as the selling price is more or less than the acquisition price. It is said, therefore, that unless the entire transaction composed of the three acts mentioned results in a gain there is, in fact, no income." See page 59 of Respondent's brief in *Goodrich* v. *United States.*

The Honorable Solicitor General went further and explained the reason for such conclusion and why he thought the Honorable Commissioner has erroneously construed the statute. He said "it (the statute) clearly emphasises the tax only on *gains* (italics his) arising from the sale of property." "It can not be said that there has been a gain resulting from a sale of propery at less than its cost." "From the beginning the income tax acts had imposed a tax only upon *gains* derived from sale."

Here we see developed by the Honorable Solicitor General and approved by this Court the theory and doctrine of reality and genuineness in gains and losses, something real, tangible and not something fanciful, invented, fabricated or fixed by fiat of the Commissioner or even of Congress itself.

The Honorable Court of Claims in both the *McKinney* and *Elmhirst* cases relied upon this doctrine of actual gain and loss as distinguished from technical or fictitious gains

or losses and cites the *Goodrich, Walsh* and *Flannery* cases, in support thereof.

In the *Elmhirst* case the court even goes further and claims that had Congress itself inserted a provision fixing the basis of value on the death of the testator that this Court would hold that merely a "limitation" which would not control as against the actual gain as shown between the purchase price and the sales price. *Elmhirst* v. *United States,* 38 F. (2d) 915, 923.

The fictitious and fabricated nature of alleged gains and losses, when we use the appraised value at date of death, finds striking illustration in both the *McKinney* and *Elmhirst* cases. In the *McKinney* case the testator had purchased the property in question for $177,130.90 prior to March 1, 1913. Its market value on that date was $187,200.00. At McKinney's death in 1918 it was appraised at $67,200.00. It was sold by the executor *for the purpose of paying debts and cost of administration* for administering the estate for the sum of $160,311.75. Thus it will readily be seen that there was no actual gain or profit or actual income. On the contrary there was a loss of some $17,000.00 between the cost and the selling price and a decrease of some $27,000.00 between the selling price and the March 1, 1913, value. Yet, in spite of this heavy actual loss—forced, it might be said by the compulsory sale of the property to pay debts and expenses of administration—the record tersely says there being no other funds available for that purpose—the Collector demanded a tax upon the difference between the selling price of $160,311.75 and the appraised value of $67,200.00, or a total tax of $34,460.25.

It is not surprising that the Honorable Court of Claims was persuaded of the artificial and fictitious nature of such a profit when a tax of over $34,000.00 was levied upon what amounted to an actual loss of $17,000.00 and that too upon

a sale in which there was no choice by the taxpayer and which was forced by the necessities of paying the debts of the estate and the expenses of administration.

The later *Elmhirst* case illustrates the same point even more vividly. In that case the original cost of the property was $2,415,248.60. The appraised value at death was $2,158,510.00. The selling price by the executor was $2,639,287.96. Thus the selling price by the executor was $224,039.36 in excess of the cost to decedent and $480,777.96 in excess of the appraised value at his death. The Commissioner assessed the tax upon this $480,777.96 and the total tax with interest so assessed was $267,033.94. In other words it was $40,000.00 over and above the entire actual gain from the sale of the property.

The imposition of such a burden upon the estate of a dead man, in one case imposing a tax of $37,000.00 upon an actual loss of $17,000.00, in the other imposing a tax of $40,000.00 in excess of the entire gain, must have shocked the conscience of the Honorable Court of Claims and almost forced upon them the conclusion that Congress could never have intended so unconscionable a result.

True, the adoption of the other basis might in some cases impose a heavy tax. Indeed, in all the cases, excepting those in the Board of Tax Appeals, adhering to the opposing rule, the holding of the Court to the rule of value at death was to relieve the taxpayer and not to favor the taxing authority.

Bankers Trust Co. v. *Bowers*, 23 F. (2d) 941.
Bingham et al. v. *Long*, 249 Mass. 79; 144 N. E. 77.

But at least in such cases there is a real, actual, tangible gain or profit which the estate enjoys; there is an actual increase of the selling price over the cost and we submit that such a burden, even though the tax may be heavy, is not unfair or unjust and is more easily to be borne than a

tax upon a mere fictitious or fabricated profit or gain which has no tangible substance in fact.

The argument has sometimes been made that it will favor some estates to have the rule of the appraised value at death adopted as the basis while in others it would work to the contrary, but this argument overlooks the crucial point and that is of real, actual, profits, as distinguished from chance or invented profits. What the argument really proves is that by adopting the rule of value at death some estates might escape paying upon their actual profits by the fortuitous circumstances of a low appraisal value at the time of death while other estates less fortunate would be required to pay upon invented profits which had no existence in fact. In other words one estate suffers a real hardship in being heavily taxed as in the McKinney estate upon actual losses or, as in the *Elmhirst* case, being taxed a sum equal to all its profit and the sum of $40,000 in addition, while other estates by the lucky circumstance of a high appraisement at death would escape being taxed upon what was an actual increase or profit over and above the original cost. The iniquity of the rule lies in the fact that in one case you tax actual losses by calling them gains and in the other case you allow actual gains to escape taxation by calling them losses and all done through the artifice of treating the substitution of the executor as representative of the estate in place of the testator, as an acquisition by such executor of the property of the estate. The result is to substitute chance, good luck, the swings of the market or fortuitous circumstances for reality, actuality and genuineness, and thus make the payment or the escape of the tax to rest upon chance and not upon the sound and honest basis of actual gains or losses.

It is this doctrine of reality, of actual gains, of something tangible, that moved the Court first in the *McKinney* case and later in the *Elmhirst* case. The very facts in the case

graphically illustrated the necessity of such a doctrine of actual gains and not fictitious gains and the court there found its reasons in the decisions of this Court starting with the *Goodrich* case. The Court of Claims says:

> "The statute, according to the construction given it by the foregoing decisions, had for its purpose the taxation of 'gains derived from the sale' of property, based on the difference between the original investment and the sale price, and the allowance of loss sustained measured in the same way. It contemplated a purchase and a sale. It made no provision, and it is clear that it did not intend, that any value other than the market value on March 1, 1913, was to be considered. Had it intended otherwise it would have so stated.
>
> "Defendant's contention in effect asks the court to add a provision to the statute to the effect that if a sale is made after the death of the purchaser and after March 1, 1913, the measure of gain or loss for the purposes of taxation should be not the measure fixed by the statute but the difference between the appraised value of the property as of the date of the testator's death and the selling price. And if this contention were sustained, it would amount to assessing plaintiffs with a taxable gain, although there was an actual loss both as between the purchase price and sale price, and the appraised value on March 1, 1913, and the sale price. The statement of the proposition is its answer.
>
> "Defendant is also contending that the sale by the executors creates a different situation from that which would have existed had the sale been made by McKinney himself, and it in effect asks the Court to consider as the cost of the property, not the purchase price, but the appraised value of it at the time of the testator's death, as though it had cost them that amount. Of course, there was no cost to the executors. They were the personal representatives of the decedent. The stock was the same stock as it had been in the hands of the decedent, and, as stated, had he lived and sold the stock himself there would have been

no question of taxable gain. The fact that they were executors did not alter the situation."

McKinney v. *United States*, 62 Court of Claims 180.

Again in the *Elmhirst* case the court emphasizes the same thought of actual gains and losses. The court there says:

"The plain theory of section 202 and the purpose in the mind of Congress was to fix definitely the basis for estimating actual profits, as distinguished from fabricated or invented profits, and for estimating the amount of profits to be taxed, and to this end it was provided that where property was acquired prior to March 1, 1913, the basis for fixing said amount was the market value of the property acquired as of that date, and thus the following clearly appears:

First. That "acquired" referred to the purchaser or owner. An executor does not "acquire" property in the sense of the purchase of it. It passes to him by operation of law. Had the purchase in the present case been made prior to March 1, 1913, it could not be contended that the executor had acquired the property as of the date of purchase or at the time the purchaser of the testator acquired it. The only person who acquired under the facts of this case was the testator.

Second. It thus appears (section 202) that the "basis" being the market value as of March 1, 1913, where the purchase was made prior thereto it could not possibly be the market value at any other time, and certainly not the value at the death of the testator. To hold otherwise would be to amend the statute. To make the value as of the death of the testator would thus be a plain alteration and change in the statute and its declared purposes, a palpable ignorement of its language and meaning.

Third. It is plain that had the property involved in this case been purchased prior to March 1, 1913, the basis for ascertaining profits would necessarily have

been held to have been its value as of that date, as fixed by the statute, thus treating the testator and his estate as a single entity and not separate entities and clearly demonstrating that as to tax on profits from the sale of property Congress so designed and intended.

The conclusion, therefore, is unescapable that in dealing with property purchased on or after March 1, 1913 (paragraph (2) of Section 202), Congress intended the same principle and rule of entity to apply when it fixed the "basis" as the "cost thereof" when "acquired," and meant "cost" at the time when "acquired" by the testator and not cost on or after his death. Any other construction does as much violence to the conceded purpose of the statute as it would to apply it to paragraph (1), section 202, and to make the basis of value of a purchase prior to March 1, 1913, the value at the death of the testator. To hold otherwise is to amend the statute and graft something on it that was not put there by Congress."

Again the court points out that had Congress meant an appraisal value it would have said so. The court says:

"The question is: How did the section provide for the ascertainment of these profits? What was the "basis" for measuring them? In the instant case the stocks were purchased after the 1st of March, 1913. Section 202 provides that "for the purpose of ascertaining the gain derived or loss sustained from the sale" of property the basis shall be "(2) In the case of property acquired on or after that date (March 1, 1913), the cost thereof; or the inventory value, if the inventory is made in accordance with section 203."

"Inventory" here mentioned deals with a trade or business and has no bearing on this case. It has, however, significance in connection with this case in that Congress in a certain class of sales departed from "cost" basis and provided the inventory value as a substitute basis for "cost" basis, indicating that in

that particular, and that particular only, was an exception to be made as to "cost" as a "basis." With that exception "cost" was to be the "basis." It could very readily have provided, if it had intended so to do, while it was making the exception in the case of a trade or business for an inventory basis, that when the property purchased was sold by the purchaser's executor after the death of the purchaser, the "basis" should be not "cost" to the purchaser but the difference between the sale price and the value of said property at the time of purchaser's death. But it did not do this and we can not supply the omission by reading into the statute something which is not there.

As the statute stands, the "basis" provided was the difference between the "cost" and the selling price, i. e., purchase and selling price (*Walsh* v. *Brewster, supra,* page 538 of 255 U. S., 41 S. Ct. 392), whether the decedent was dead or alive. Of course, Congress knew that people die and that very often property passing to an executor is thereafter sold, and in the light of this knowledge could have provided for another basis than the one provided by this section, but this it did not do.

We hold in this case, as we held in the *McKinney* Case, that under section 202 the basis provided for ascertaining loss or gain from the sale of property is the difference between the "cost" or purchase and the selling price.

The regulations fixing the appraised value at death for estate tax as the "basis" instead of "cost," named in said section, was an attempt to add a provision to section 202 that it did not contain. It was an attempt to "graft something on the statute that was not there," *Smietanka* v. *First Trust & Savings Bank,* 257 U. S. 602, 42 S. Ct. 223, 224, 66 L. Ed. 391, something that was not within the express contemplation of the statute."

Elmhirst v. *United States,* 38 F. (2d) 915.

Nearly all the Courts adopting the opposing rule, including the Circuit Court of Appeals in the case at bar, have attached great importance to the decision of the Massachusetts Supreme Court in the case of *Bingham* v. *Long*, cited above, in which that Court under its state statute adopted the value at the death of the decedent to escape the imposition of a heavy tax upon an estate but both the Massachusetts income tax law, as well as the relationship of the executor to the estate are peculiar and the connection of the executor and the beneficiary different from that of common law in which the executor is the representative of the deceased acting as an officer of the Court to settle up the estate, pay the debts and sell such property as is necessary for paying the debts and expenses of administration.

The Massachusetts Court says:

> "Although the tax is exacted in these instances from the executor, administrator, or trustee, the person upon whom the burden of the tax fairly rests is the beneficiary, and *whether the tax shall be levied at all depends upon the residence of the beneficiary.*"

And again:

> "The mere fact that the residence of the decedent was within the commonwealth does not, under general principles of law, render his personal estate subject to taxation here, where such estate is not actually within the commonwealth, and the executor or administrator, who is its owner is a non-resident."

We submit that these two quotations show that the Massachusetts law is peculiar to itself and that undue weight has been attached to this decision by outside Courts.

The Honorable Circuit Court of Appeals was impressed with the argument that inequality would arise in relation to the inheritance tax upon estates and that the rule contended for by petitioner would result either in a double

tax or escape, partially or entirely, from taxation. The Honorable Court of Claims has already pointed out in the *Elmhirst* case the difference between the inheritance tax statute and the income tax statute and that the two relate to entirely different matters and that discussion leaves the question without necessity for extended comment here. When we consider that the inheritance tax is based upon the net estate after the payment of all debts, expenses of administration and other charges and has an additional exemption of $50,000.00, it seems to us that the argument of the Honorable Circuit Court has but slight application. There are too many factors involved. Too often the income tax would have to be paid whether there was an inheritance tax or not, as the latter is dependent upon too many factors. We have only to apply the argument of the Honorable Circuit Court to the actual facts in the *McKinney* and *Elmhirst* cases to see that its application is too uncertain, too contingent, too difficult, to anticipate and forecast, to make it of any value in interpreting the mind of Congress in passing the statute making an executor a taxpayer. And whatever might be the effect of the income and the inheritance tax operating together, we would at least be dealing with reality, with actual profits and actual losses, with actual value, actual increase and decrease in the estate.

Again the adoption of the rule of cost to the testator includes the profits and likewise the losses between the time of purchase and the date of the death of the testator and so avoids the hiatus during that time, a thing necessarily to be desired, for under the rule contended for by the Commissioner the profits from the date of purchase to the death of the testator could not be taxed, save in the exceptional case where they might or might not be reached by some inheritance tax.

In the *Brewster* v. *Gage* case one of the convincing arguments advanced by the Government to make the date of

acquisition of the heir the date of death of the testator and not the date of the final decree, was to avoid this hiatus and to reach the profits during such time.

The regulations of the Department throw no light upon the question as they have varied with the decision of the Court.

We respectfully represent to the Court that there is also a vital distinction and a vital necessity to use a different basis between a sale by heir or legatee and a sale by an executor. The executor is not the representative of the heir. Very often his position is antagonistic to the heir. He is the representative of the deceased, to see that the deceased's debts are paid, his estate conserved and properly administered and, if necessary, as in the *McKinney* case, to sell the property to pay the debts and expenses of administration, to pay the various taxes, state and Federal, and when all this is done to turn over the residue to the heir or legatee. The statute governing a sale by an heir specifically provides that the basis for the sale is acquisition value while the statute applicable to the uses, the general expression of a taxpayer, to-wit: Cost or March 1st, 1913 value. Of course, the heir acquires the property on the death of the testator. He comes into a new ownership, a new acquisition, something he never owned before and subject only to the requirements of administering the estate and there is not the same continuity as there is between an executor and the testator. The executor in the language of the Court of Claims stands in the shoes of the testator and winds up his business, pays his debts and distributes the residue. Again, the sale by an heir or legatee is voluntary. He can choose his time, place and occasion, while the sale by an executor is almost invariably involuntary under the order of the Court, forced by the compelling need of raising funds to pay the debts of the decedent. The executor has no choice but to sell the assets and pay

the debts and he often has little choice as to the time of sale.

We submit that necessity, reason, justice and the circumstances surrounding estates call for a distinction between a sale by an executor and a sale by an heir.

The Honorable Court of Claims found no difficulty in distinguishing between the sale by an heir and a sale by an executor.

See *Myers* v. *United States,* 51 F. (2d) 45.
McCann v. *United States,* 48 F. (2d) 446.

In conclusion we submit that the rule laid down by the Honorable Court of Claims, of cost to the testator, is the true basis for determining gains and losses, that it is based upon actual gains as distinguished from fabricated gains. That to interpret the Act of Congress as taxing gains which did not exist, which have no substance, which are pure figment of the law would make the Act of Congress beyond the limitations of the 16th Amendment and in violation of the Constitution of the United States as an attempt to tax as income something which was not income.

Respectfully submitted,

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